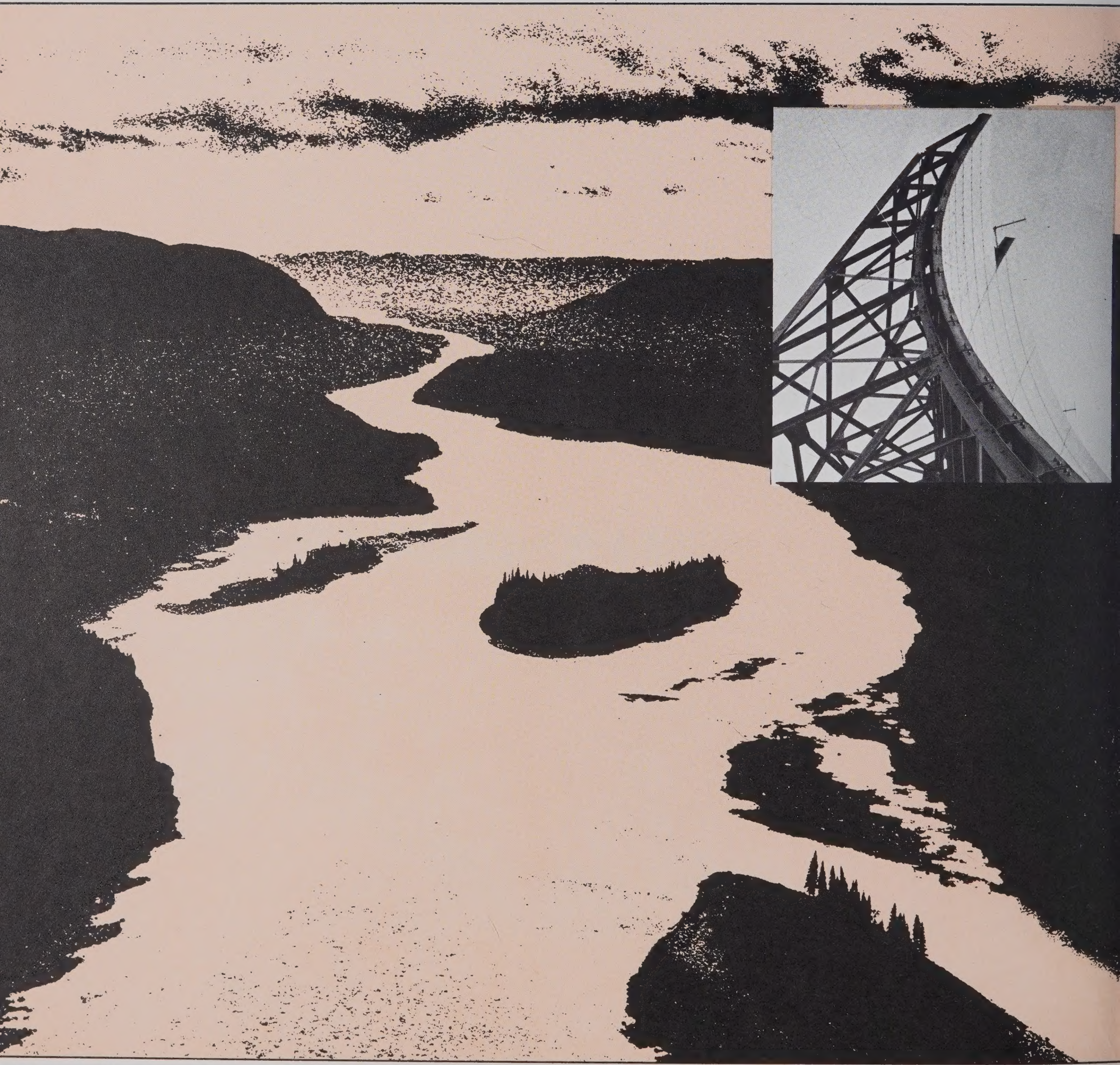
Newfoundland Telephone Company Limited Annual Report 1975

The abundance of hydro power—particularly from Labrador's Churchill River—and a wealth of other natural resources make Newfoundland a most desirable location for new industry.

As Newfoundland grows, so does the demand for high-quality telecommunications. This is particularly true of Labrador where the tropospheric scatter system (below) has played a significant role in communicating across the vast distances of Labrador. Improvements such as the recently completed Goose Bay to Nain microwave will serve to bring this important region into the telecommunications mainstream of the province.



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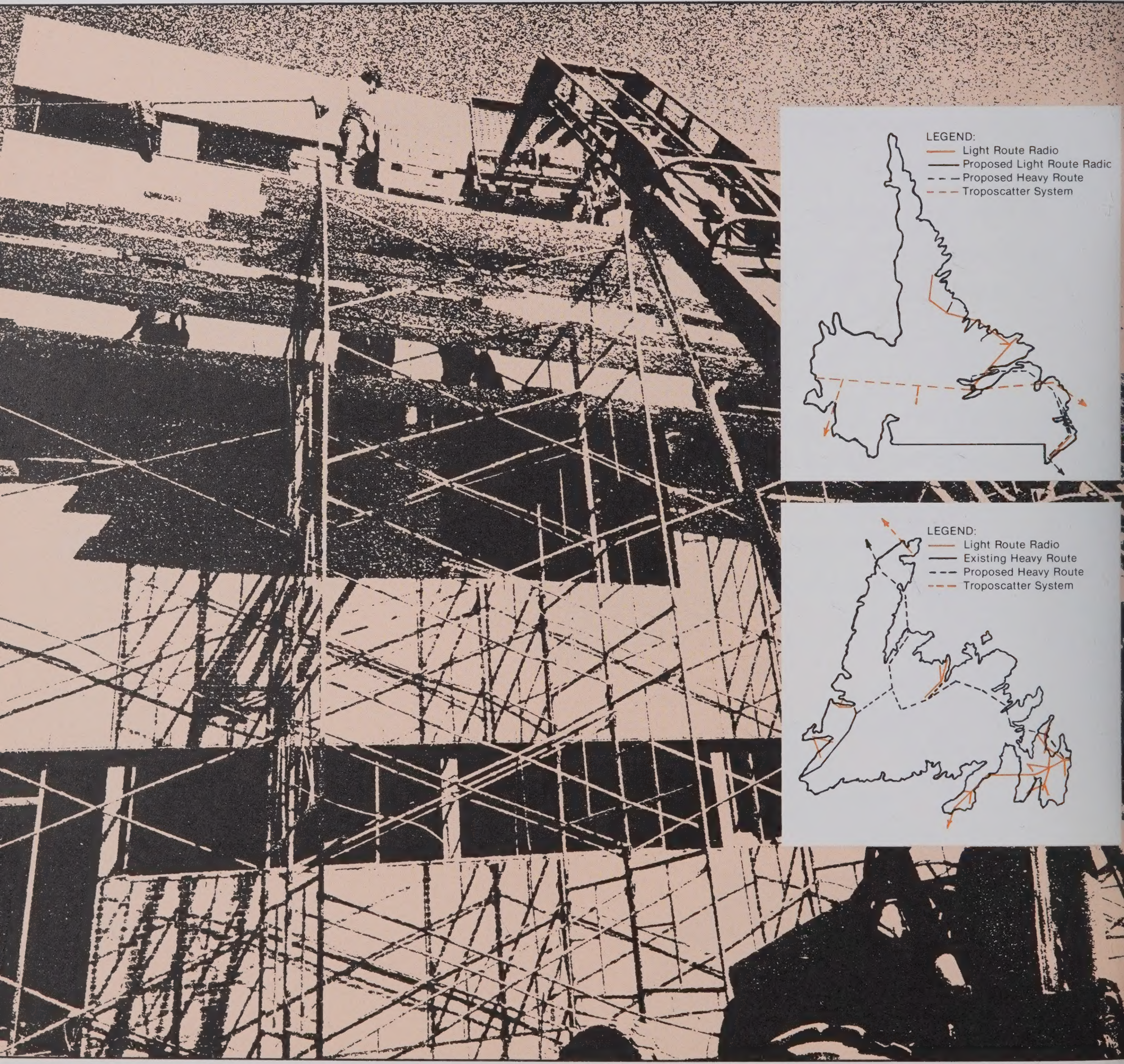
The construction industry is currently the largest goods-producing industry in the province. Major projects presently under construction, or scheduled to begin in the near future, include the $59 million health sciences teaching complex at Memorial University (shown below), as well as new schools, hospitals, industrial parks and housing developments.

Newfoundland Telephone's operating territory contains 77% of the province's population, and most of its urban and industrialized centers. The company is committed to building the strong and efficient communications network which is vital to the province's development.



Newfoundland Telephone Company Limited

Newfoundland, the most easterly province of Canada, includes two distinct geographical areas: the island of Newfoundland in the Gulf of St. Lawrence, and the mainland Labrador region.

At the time of Confederation with Canada in 1949, Newfoundland was less developed than other provinces. Since then, there has been extensive growth and development in the provincial economy. The Gross Provincial Product, which was $200 million or $580 per capita in 1949, had grown to $2,026 million or $3,738 per capita by 1974.

The economic structure has undergone considerable change in the last 25 years. Once almost wholly dependent on the traditional fishing industry, the economy has been strengthened and diversified by rapid developments in other resource-based industries. Continuing expansion in mining and energy is expected to make these industries the most valuable in the economy, followed in importance by construction and manufacturing.

The province is linked to the rest of Canada by regular air service, a trans-island bus and rail freight system, and car and passenger ferries. The telephone system provides a more immediate link, which is increasing in importance as transportation costs continue to soar.

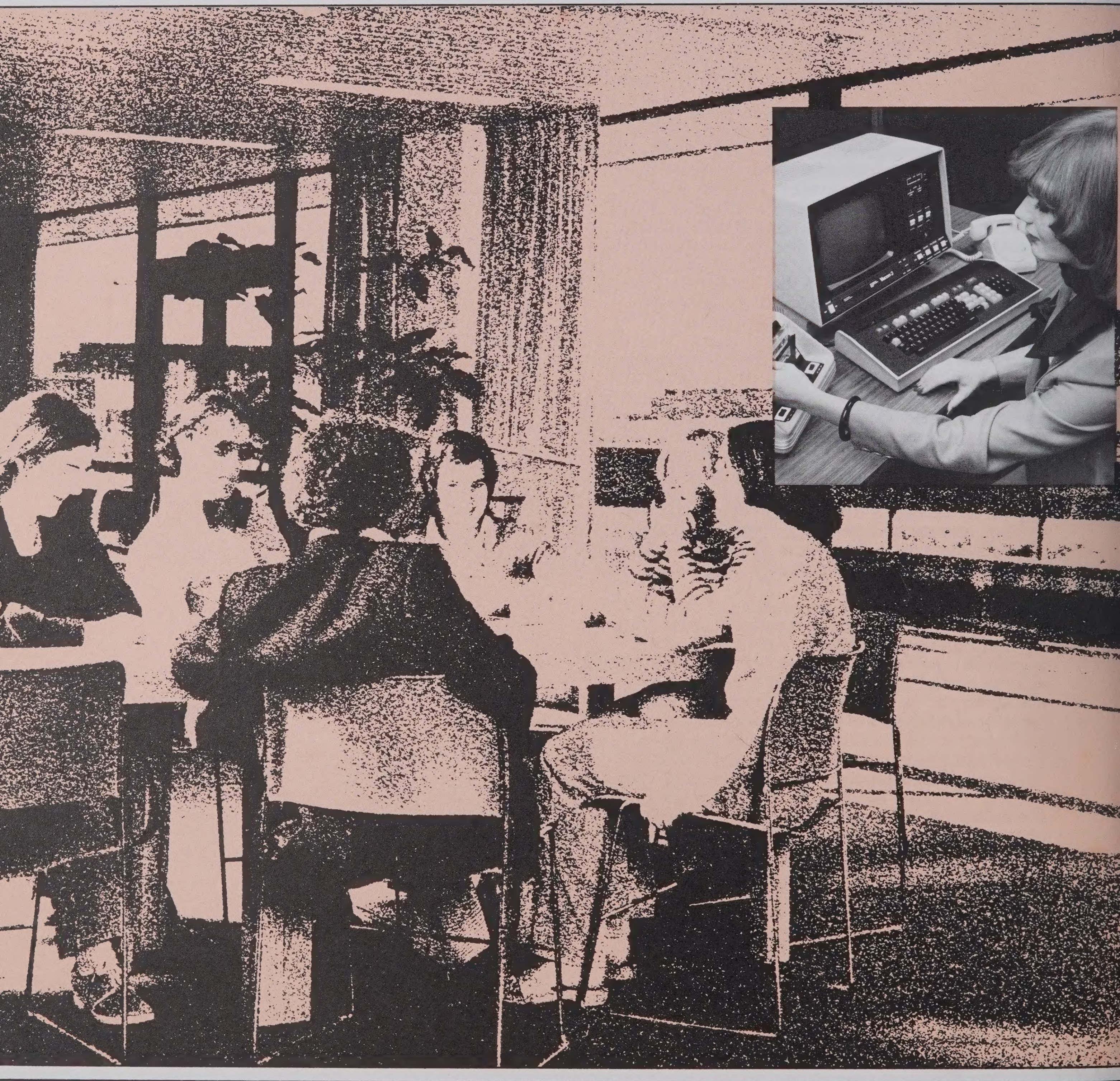
The population of the province as of July 1, 1975 was 550,000, 77% of which resides in areas served by Newfoundland Telephone. About 41% of the population resides on the Avalon Peninsula in the eastern part of the island, which includes the capital city of St. John's. The Company's operating territory comprises the entire Avalon Peninsula, the southern part of the Burin Peninsula, the Grand Falls-Point Leamington area in central Newfoundland, the south-west coast of the island including the city of Corner Brook, and all of Labrador with the exception of Labrador City. Two other telephone companies operate within the province: Canadian National Telecommunications, and the Labrador City Telephone Company.

At December 31, 1975, Newfoundland Telephone had 150,389 telephones in service, all of which were dial. Approximately 71% of these were residence telephones.

Long-distance service—both operator-handled and Direct Distance Dialed—is provided to subscribers over a network of owned and leased transmission facilities. Newfoundland Telephone has already completed the first phase of its own cross-island microwave system, which will accommodate growth of this traffic in future years. The Company is a member of the Trans-Canada Telephone System, (TCTS) a consortium of Canada's major telephone companies, which operates a cross-country communications network for the transmission of data, TV, AM and FM broadcasting, and regular telephone traffic. Through TCTS, the Company has access to the national market, and shares in the revenues of inter-province communication both to and from Newfoundland.

The inset shows the operation of a Vucom 3—a sophisticated computer terminal, which is part of the various business communications systems offered by Newfoundland Telephone.

Designing and installing systems to meet the particular needs of an organization is a highly demanding, technical job. Similar challenging positions exist in all parts of the Company. Increasingly, the Company has come to rely on the talents of Newfoundland's young people. Graduates of Memorial University, as well as the many vocational schools and colleges in the province, have the skills and enthusiasm essential for the advancement of the telecommunications industry.



1975 Highlights

Summary of Revenues and Expenses

	Year 1975	Year 1974*	Changes
Revenues			
Local Service	$16,355,044	$13,793,190	$2,561,854
Long Distance Service	26,389,215	21,459,884	4,929,331
Miscellaneous Income—Net	979,396	871,600	107,796
Total Revenues	43,723,655	36,124,674	7,598,981
Expenses			
Operating Expenses	29,382,155	24,214,269	5,167,886
Income Taxes	2,016,424	1,550,524	465,900
Debt Charges	7,106,774	5,599,005	1,507,769
Total Expenses	38,505,353	31,363,798	7,141,555
Net Income for the Year	$ 5,218,302	$ 4,760,876	$ 457,426

Rate Relief:
Decisions of the Board of Commissioners of Public Utilities of Newfoundland.

Jan. 15—Allowed a rate of return on rate base of 10.1% producing 22% of the additional revenues requested.

April 7—Approved Company's request in full generating approximately $1.5 million additional revenues in 1975.

Nov. 19—Allowed 67% of the revenues requested producing an additional $200,000 in 1975 and an estimated $3.1 million in 1976.

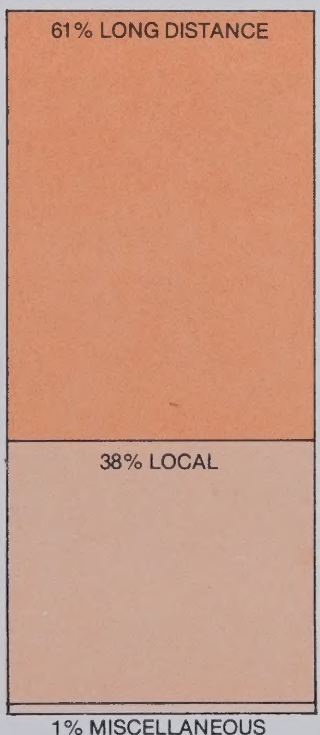
The Board also endorsed a rate of return on rate base of 10.4—10.7% with a return on common equity of 14—15%.

Financial Results:
Total revenues increased by 21.0%.
Total expenses rose by 22.8%.
Construction expenditures amounted to $27,323,473.
Investment in plant and equipment reached $169,422,806.
Rate of return on average total capital was 10.10%.

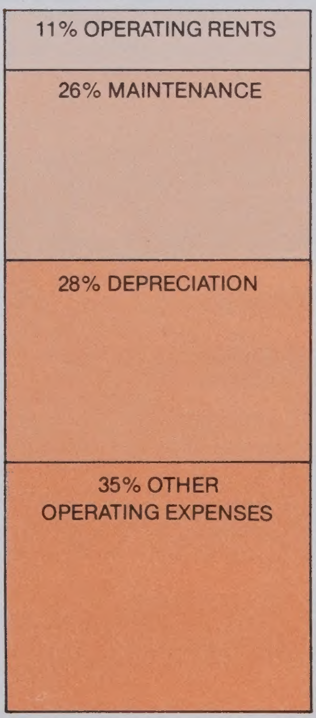
Expansion:
Long distance calls increased 16.7% to total 11,094,229. Telephones increased 6% to total 150,389. Last dial conversion completed making company 100% dial operation.—First phase of the cross-island microwave completed.

*1974 figures have been restated for Income Tax reduction of $255,643.

Breakdown of Operating Revenues 1975



Breakdown of Operating Expenses 1975



"The Company's growth during the year was accomplished in the face of mounting costs and an increasing demand for service. ...Internal restrictions on spending meant increased pressures on Newfoundland Telephone's 1278 employees. The Board of Directors extends its sincere appreciation for their efforts in coping with the challenge, and making 1975 a year of overall success."

A.A. Brait

President's Message

Newfoundland Telephone's earnings in 1975 were maintained at substantially the same level as recorded a year earlier. The fact that this was accomplished in the face of cost increases never before experienced by the Company and in a generally sluggish economy is a tribute to the initiative and dedication of all our employees.

Total revenues for the year grew by 21.0% while total expenses rose by 22.8%. Earnings per common share were 85 cents.

Although a reduction in economic activity was reflected in a modest 5.9% increase in the number of telephones added to the system this year, the healthy expansion in long-distance usage was encouraging. This year close to 1.6 million more calls were placed than the year before, an increase of 16.7%.

It became evident early in the year that a concerted effort to control and cut expenses as well as to reprice our services was required. The success of these efforts has been reflected in the substantially improved performance in the second half of 1975 and is a measure of your Company's ability to respond to adverse conditions.

Utilizing a 10.1% rate of return on rate base granted earlier by the Board of Commissioners of Public Utilities of Newfoundland, a February 7th application for increased rates was completely successful and generated approximately $1.5 million in additional revenue during 1975.

Since this only partially offset the effects of inflation and the need was still evident to provide a level of earnings which would attract investment to support the telecommunications needs of a growing province, the Company submitted a new application to the Board on August 18. The Company was granted 67% of the revenues requested, but more importantly was allowed a rate of return on common equity of between 14 and 15%.

The Board's decision acknowledges that in order to provide the high quality of service that our customers require the Company must be given a real opportunity to earn a return which will be attractive to investors in today's market.

In rejecting a proposed Cost of Service Adjustment, the Board agreed that the use of an estimated test year would result in a better balance between revenues and expenses in a period of rapid inflation, but believed this would be contrary to the Public Utilities Act. The Board further stated that the recommendation to seek an amendment to the Act will be taken into consideration.

Among the major events that highlighted the year's activity was the completion, in December, of the first phase of the cross-island microwave. This section extends from Corner Brook to Cape Anguille and then by a 78 mile over-water span to a similar system provided by Maritime Telegraph and Telephone near Sydney, Nova Scotia. Approximately $2 million was spent on the Newfoundland portion of the project in 1975. The system will effectively extend our capacity to handle the rapidly expanding toll, broadcast, and data markets.

A second microwave system, this time in Labrador, successfully brought the people in more remote sections of the region into the mainstream of modern telecommunications. The system, connecting Goose Bay to Hopedale and Nain represents a significant portion of the Company's three year improvement plan for the area. The plan is on schedule and will be completed in 1976.

In May we achieved our objective of 100% dial operation when the exchange area of Witless Bay was provided with a $1.1 million electronic switching office. Coincident with the provision of dial service, Direct Distance Dialing was also introduced.

In St. John's, work proceeded during the year on a new electronic switching office designed to serve the provincial and federal governments as well as other major businesses. To date $4.1 million has been spent on the project which will provide these organizations with a full spectrum of business services and meet their future requirements for the most modern voice communication facilities available.

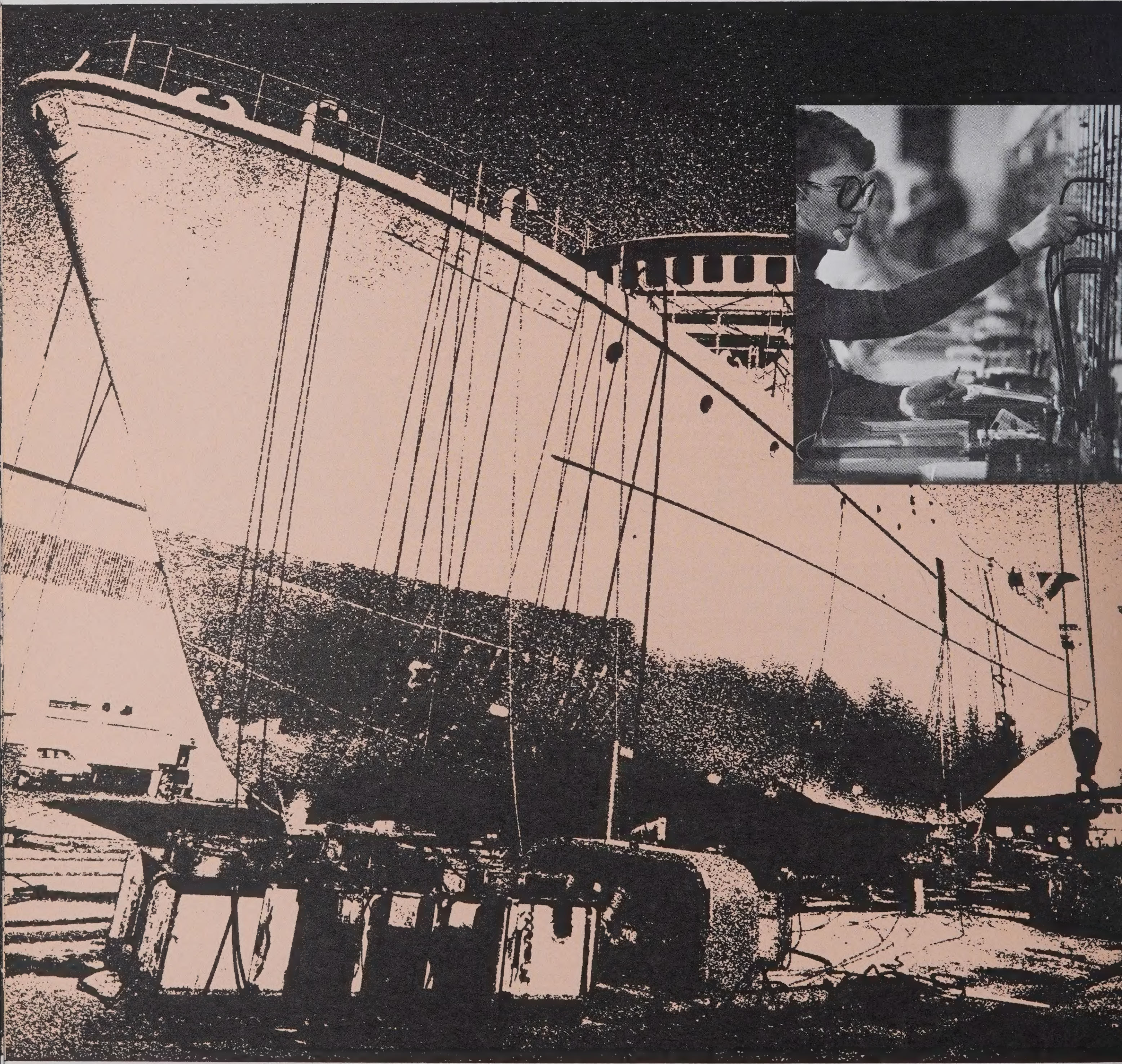
In order to safeguard the long term health of the enterprise, the Company must plan for a continuing high level of capital expenditure. The efficient utilization of capital will therefore demand our greatest attention.

In the coming year we are committed to achieving the earnings which will attract investment on good terms, offering the highest possible quality of service and providing challenging and satisfying work for our employees. There is no doubt that 1975 has provided a firm base from which we can confidently pursue our goals for 1976.

A. A. Brait

Newfoundland's wealth of natural resources provides a sound base for a variety of manufacturing and processing industries. The Marystown shipyard (below) is one example. Others include pulp and paper companies at Grand Falls, Corner Brook and Stephenville, and many fish processing plants throughout the province.

Essential to the efficient operation of thes industries, Newfoundland Telephone's long-distance network provides the communications link for most businesses in the province. The company handles an average of 30,395 long-distance calls per day.



1975, with its uncertain economic conditions and extremely high rate of inflation, was a difficult year for most Canadian businesses.

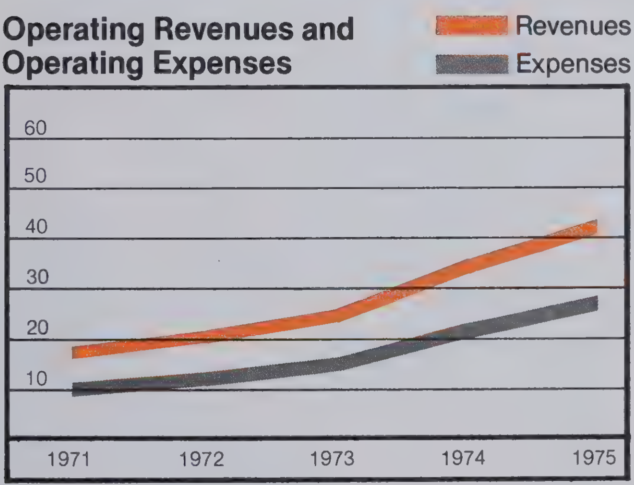
The Company's growth during the year was accomplished in the face of mounting costs and an increasing demand for service. In spite of these difficulties, revenues rose to a satisfactory level toward year-end; and resulted in a financial position very similar to that recorded in 1974.

Internal restrictions on spending meant increased pressures on Newfoundland Telephone's 1278 employees. The Board of Directors extends its sincere appreciation for their efforts in coping with the challenge, and making 1975 a year of overall success.

The Battle against Inflation

Throughout the first half of the year, the Company's operating expenses rose at a much faster pace than revenues. Most items in the $27,323,473 construction program rapidly increased to a much higher cost than had been anticipated. To combat these trends an internal cost-cutting program was instituted; and, by the third quarter, the increases had been significantly reduced.

Operating Revenues and Operating Expenses



However, growth was sluggish in some sectors. Discounting the addition of some 8638 telephones in Labrador to the system, the telephone gain for 1974 was 8.3% over the preceding year. In 1975, the rate of increase was only 5.9%.

Growth in toll usage, however, was encouraging. Completed toll messages for the year totalled 11,094,229—a 16.7% increase over 1974. The interruption of postal service during the fourth quarter resulted in an abnormally sharp increase in calling, as the public searched for a practical alternative to communication by mail.

Total expenses for the year came to $38,505,353, a 22.8% increase over the previous year; while revenues increased 21.0% for a total of $43,723,655. Net income for the year was $5,218,302.

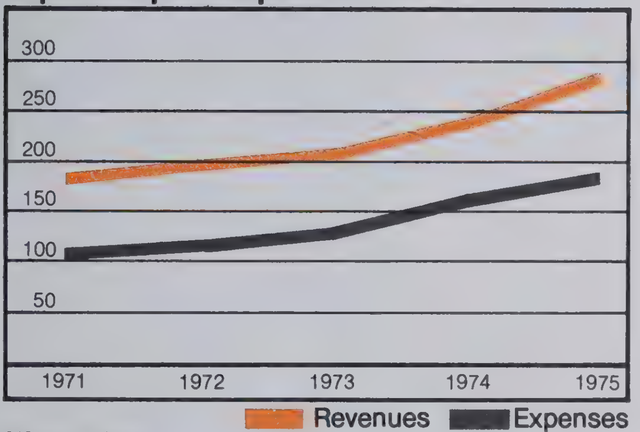
Rate Relief Granted

A major factor contributing to the satisfactory level of growth in earnings in the latter part of the year was the rate relief granted by the Board of Commissioners of Public Utilities. In January, minimal increases were granted by the Board, amounting to less than 1.4% of actual 1974 revenues. This represented a very small percentage of the amount requested. To add to the difficulty, expenses had continued to soar between the time of application and the time the Board's decision was made. It became evident that further relief would be required. In February, the Company reapplied to the Board, asking that the previously allowed rate of return be applied to year-end figures in order to take growing expenses into account. This application was approved in its entirety.

Nevertheless, earnings were not yet at a level that could satisfactorily attract investment capital. An August rate increase, governing long-distance calls between companies of the Trans-Canada Telephone System, helped only slightly to meet this need. It became apparent that further increases were urgently required and on August 18th, the Company again applied for an increase in rates. The Board's decision in November allowed a rate of return of 10.4 to 10.7% on the rate base, and a return on common equity of between 14 and 15%.

The Avalon Mall in St. John's is one of the major retail shopping centers in the province.
The need for fast, efficient communications—with the public, with suppliers, and with branch outlets—is one of the major requirements of the retail trade. Newfoundland Telephone fills this need with a wide variety of special equipment for business use. Private switchboard systems, such as the one shown in the inset, are very widely used by larger firms. The Company also provides facilities which can link an organization in Newfoundland to a data processing center anywhere in Canada.

Operating Revenues and Operating Expenses per telephone Dollars



Financing

In May, 1975, the Company issued $9 million in Cumulative Redeemable Preferred Shares at a dividend rate of 9¾%.

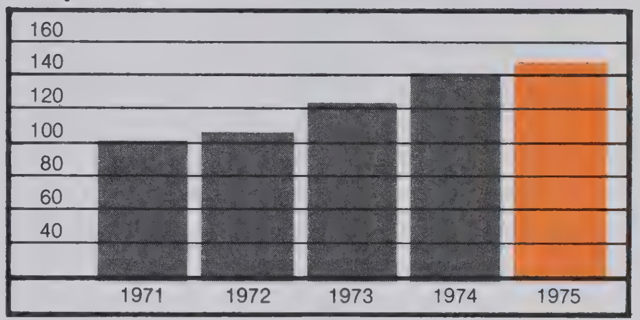
Although inflation is expected to continue during 1976, it is anticipated that the government's anti-inflation program along with a program of restraint in all sectors of the Company's operations, will be effective in keeping costs down to a tolerable level. Under these conditions, the new rate structure should provide a sound basis of growth in earnings in the new year.

Partial financing for 1976 has been completed, with a $10 million private placement of First Mortgage Sinking Fund Bonds at an interest rate of 11½%.

Service Development

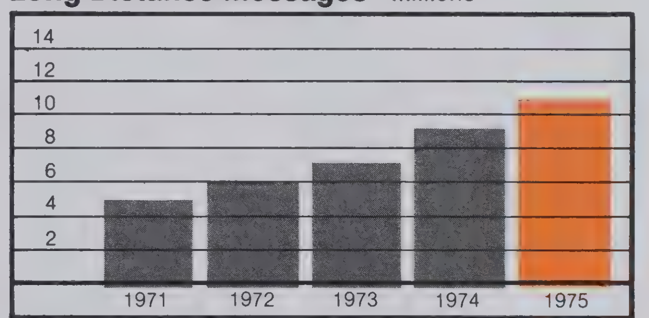
A long-standing objective was reached in May, with the provision of automatic dial service to several small east-coast communities in the Witless Bay area. The project marked the completion of the Company's dial-conversion program, begun in 1967. Telephones in our operating territory are now 100% dial; and 97% of these are private-line telephones.

Telephones in Service Thousands



The first phase of the Company's cross-island microwave system was also completed in 1975. At year-end, the system stretched from Corner Brook to Cape Anguille, and overwater to Sydney. The system will provide the increased toll capacity needed to cope with the growth in public demand for long-distance service.

Long Distance Messages Millions



A second microwave system was constructed during the year, providing high-quality long-distance service from Goose Bay to the Labrador coastal communities of Hopedale, Makkovik, Postville, and Nain. Part of the Labrador Improvement Program undertaken in 1974, the 280 mile-long microwave replaces the high-frequency radio system previously serving these communities. By relieving the load on the radio circuits, communities still operating on the high-frequency system will also enjoy better service.

Over 70% of the telephones operated by the Company are residence telephones; and, as of 1975, 100% of them are dial.

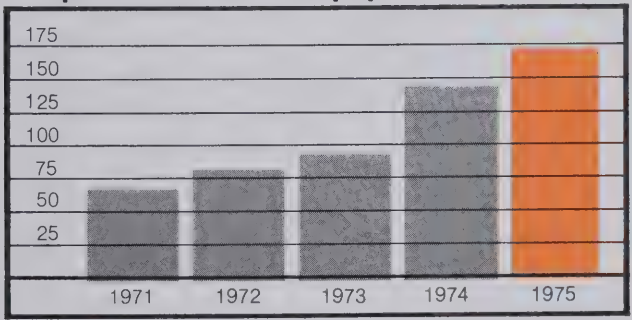
The residence market is provided with the same high level of service as the business community— including access to the Direct Distance Dialing network in most areas. Much of the construction activity carried on by the Company is geared toward improving and expanding basic service to residence customers in every area of the province, and meeting their growing demand for dependable long-distance service.

Several major projects were under construction at year-end. In February, 1976, a modern electronic local switching system called CENTREX will provide improved modern telecommunications for the provincial and federal governments as well as other major business customers in St. John's. With CENTREX, callers—whether local or long-distance—will be able to dial directly to any extension in the system, without first going through the switchboard. Outgoing and internal calls can also be dialed directly. The result will be a substantial reduction in the number of switchboards and in the cost of operator services—as well as the increased accessibility of government to the public. The system provides the capability to keep pace with the expanding needs of St. John's major businesses.

The installation of a long-distance electronic switching office in St. John's is planned for completion in December of 1976. This new facility will handle all long-distance switching in the eastern Newfoundland area, freeing existing equipment to provide local switching services. The installation of this office will also enable the Company to provide Direct Distance Dialing to customers in the Bay Roberts exchange—the last office on the island portion of the province to receive this service. The Allandale building, which is the Company's main office in eastern Newfoundland, was expanded during the year in preparation for the installation of both local and long-distance electronic switching offices. The expansion included the construction of a third story, resulting in the provision of an additional 25,000 feet of floor space.

Telephone Plant and Equipment

Millions of Dollars



Other plans include the construction of a Labrador microwave system during 1976, which will stretch from L'Anse au Loup through Mary's Harbour to Charlottetown. Part of the Labrador Improvement Program, this project will fulfill present needs in many Labrador communities, as well as making adequate provision for future growth.

Vucom 3 Introduced

A new visual display data communications terminal, Vucom 3, was introduced to Newfoundland customers in October. Designed by the Computer Communications Group of the Trans-Canada Telephone System. Vucom 3 is equipped with a micro-computer and an advanced system of self-diagnostics.

Professionals in the data field from all parts of eastern Canada attended a display of Newfoundland Telephone's service offerings in August, when St. John's hosted the Data Processing Management Association Convention.

With the help of representatives of the Trans-Canada Telephone System, the Company set up and staffed the display, demonstrating our ability to service both the national and local data markets.

Company Reorganization

In October, a detailed plan for reorganization of the Company received the approval of the Resources Committee of the Board of Directors.

The plan, which will be implemented in 1976, will group employees according to the task to be accomplished, rather than by similarity of skills. It is a basic move from the 'traditional' structure into a modern 'work flow' system. This change is part of a concerted program to serve the customer better and improve the efficiency of the Company's operation.

The unprecedented growth in workload necessitated a restructuring of the Accounting Department in April, 1975. D. Adey assumed the new position of Treasurer and Assistant Secretary; while D.G. Wright replaced Mr. Adey as Comptroller. Both Mr. Adey and Mr. Wright are officers of the Company.

Balance Sheet

Assets

	December 31 1975	December 31 1974*
Telecommunications Property (Note 2)		
Buildings, plant and equipment	$158,330,169	$138,266,131
Less: Accumulated depreciation (Notes 1 and 3)	43,110,793	38,226,396
	115,219,376	100,039,735
Land and plant under construction—at cost	11,092,637	8,077,828
Materials and supplies, at lower of cost and net realizable value (Note 1)	2,238,950	2,146,325
	128,550,963	110,263,888
Investment (shares in Telesat Canada—at cost)	300,000	300,000
Current Assets		
Short term investment—at cost	—	1,000,000
Accounts receivable—principally from customers and agents	8,058,427	6,172,851
Prepayments	377,257	287,693
Income taxes recoverable	—	2,042,965
	8,435,684	9,503,509
Deferred Charges		
Unamortized deficiency in accumulated depreciation (Notes 1 and 3)	899,100	974,025
Unamortized expenses (Notes 1 and 4)	83,776	167,551
Unamortized long term debt expenses (Note 1)	1,045,665	1,229,742
Other (Note 1)	1,202,414	980,294
	3,230,955	3,351,612
	$140,517,602	$123,419,009

*Restated—see Notes 6 and 10

On behalf of the Board of Directors:
F.A. O'Dea, Director
H. Collingwood, Director

Liabilities and Shareholders' Equity

	December 31 1975	December 31 1974*
Shareholders' Equity		
Preferred shares (Note 5)	$ 13,517,800	$ 4,784,500
Ordinary shares (Note 5)	25,411,295	25,411, 295
Premium on ordinary shares	775,987	775,987
Capital redemption reserve fund (Note 5)	482,200	215,500
Retained earnings (Note 6)	8,582,997	7,327,453
	48,770,279	38,514,735
Unsecured Subordinated Notes—Due to Parent Company (Note 7)	9,649,941	10,779,941
Long Term Debt (Note 8)	53,751,000	60,365,000
Notes Payable (Note 9)	18,200,000	4,100,000
Current Liabilities		
Bank advance	1,300,020	958,080
Accounts payable	1,684,063	2,048,308
Due to parent company	290,952	441,236
Due to affiliated companies	778,543	1,772,324
Advance billing for service	546,383	428,368
Taxes accrued	422,527	427,299
Interest accrued	873,928	864,588
Dividends payable	49,506	14,700
	5,945,922	6,954,903
Deferred Income Taxes (Notes 1 and 10)	4,200,460	2,704,430
	$140,517,602	$123,419,009

*Restated—see Notes 6 and 10

D.G. Wright, Comptroller

Income Statement

	Year 197[illegible]	Year 1974*
Operating Revenues		
Local service	$16,355,044	$13,793,190
Long distance service	26,389,215	21,459,884
Miscellaneous—net	348,785	254,642
Total Operating Revenues	43,093,044	35,507,716
Operating Expenses		
Depreciation (Notes 1 and 3)	8,274,216	6,834,471
Maintenance	7,507,303	6,429,412
Operating rents	3,378,654	2,520,230
Other operating expenses	10,221,982	8,430,156
Total Operating Expenses	29,382,155	24,214,269
Net Operating Revenues	13,710,889	11,293,447
Other Income (Note 11)	630,611	616,958
Income Before Underlisted Items	14,341,500	11,910,405
Interest Charges		
Interest on long term debt	5,143,005	4,041,449
Other interest	1,963,769	1,557,556
Total Interest Charges	7,106,774	5,599,005
Income Before Income Taxes	7,234,726	6,311,400
Income Taxes (Notes 1 and 10)	2,016,424	1,550,524
Net Income	5,218,302	4,760,876
Dividends on Preferred Shares	908,089	352,404
Net Income Applicable to Ordinary Shares	$ 4,310,213	$ 4,408,472
Earnings per Ordinary Share (based on average number of shares outstanding)	$0.85	$0.87

*Restated—see Note 6

Statement of Retained Earnings

	Year 1975	Year 1974
Balance at Beginning of Year :		
As previously reported	$ 6,604,349	$ 5,117,649
Adjustments of prior years' income taxes (Note 6)	723,104	467,461
As restated	7,327,453	5,585,110
Net Income	5,218,302	4,760,876
	12,545,755	10,345,986
Deduct:		
Dividends		
Preferred shares	908,089	352,403
Ordinary shares	2,541,130	2,541,130
	3,449,219	2,893,533
Transfer to capital redemption reserve fund	266,700	125,000
Expenses on issue of preferred shares (net of income tax reduction of $142,031)	246,839	—
	3,962,758	3,018,533
Balance at End of Year	$ 8,582,997	$ 7,327,453

Statement of Changes in Financial Position

	Year 1975	Year 1974*
Source of Funds		
Operations		
Net income	$ 5,218,302	$ 4,760,876
Items not requiring current funds		
Depreciation and miscellaneous	8,104,224	6,568,886
Deferred income taxes	1,496,030	1,552,273
	14,818,556	12,882,035
Net proceeds from notes payable	14,100,000	3,600,000
Proceeds from preferred share issue	8,724,786	—
Proceeds from issue of long term debt	—	17,127,231
Proceeds from subordinated notes	—	10,779,941
Decrease in working capital	58,844	—
	$37,702,186	$44,389,207
Disposition of Funds		
Construction expenditures		
Gross construction expenditures	$27,323,473	$28,614,346
Deduct: Charges to construction not requiring an outlay of funds	(1,232,434)	(838,321)
Increase in materials and supplies	92,625	47,905
	26,183,664	27,823,930
Acquisition of telecommunications property in Labrador (Note 2)	—	11,741,648
Dividends—Preferred	908,089	352,403
—Ordinary	2,541,130	2,541,130
Repayment of subordinated notes	1,130,000	—
Repayment of long term debt	6,614,000	439,000
Redemption of preferred shares	266,700	125,000
Miscellaneous	58,603	399,580
Increase in working capital	—	966,516
	$37,702,186	$44,389,207
The increase (decrease) in working capital is accounted for by:		
Increase (decrease) in current assets:		
Short term investment	$(1,000,000)	$ (772,748)
Accounts receivable	1,885,576	1,955,528
Prepayments	89,564	(32,068)
Income taxes recoverable	(2,042,965)	1,292,640
(Increase) decrease in current liabilities:		
Bank advance	(341,940)	1,035,891
Accounts payable	364,245	(135,215)
Due to parent company	150,284	(275,296)
Due to affiliated companies	993,781	(1,506,425)
Advance billing for service	(118,915)	(78,672)
Taxes accrued	4,772	(55,654)
Interest accrued	(9,340)	(461,520)
Dividends payable	(34,806)	55
	$ (58,844)	$ 966,516

*Restated—see Notes 6 and 10

December 31, 1975

1. Summary of accounting policies

Depreciation

Depreciation is computed on the straight-line method using rates based on the estimated useful lives of the assets. When depreciable telecommunications property, other than minor items thereof which are replaced, is retired, the amount at which such property has been carried in telecommunications property is charged to accumulated depreciation (see Note 3).

Materials and Supplies

Materials and supplies consist of items which will be used in the construction program and are valued principally at average cost.

Income Taxes

Deferred tax accounting has been followed with respect to timing differences other than those related to differences between capital cost allowances and depreciation (see Note 10).

Deferred Charges

Expenses incurred for other than long term debt are being amortized as ordered by the Board of Commissioners of Public Utilities of Newfoundland (see Notes 3 and 4).

Expenses incurred in connection with the issue of long term debt are amortized on a straight-line basis over the life of the debt.

2. Telecommunications property

Telecommunications property consists of land, buildings, plant and equipment including poles, wire, cable, underground conduit, microwave radio relay equipment, telephone apparatus, motor vehicles, office furniture, other miscellaneous equipment and construction in progress. Telecommunications property was valued, as at December 31, 1963 by Bell Canada after a complete physical inventory substantially on the basis of actual cost but where necessary on developed unit costs for each year of placing. Subsequent additions are at cost except as stated below.

On January 1, 1974, the Company purchased from Bell Canada, its Parent Company, the telephone plant and certain other assets comprising Bell Canada's telecommunication system in Labrador. These assets have been recorded in the Company's books of account substantially at their original cost of $26,660,248 less the accumulated depreciation to December 31, 1973 of $13,912,726. Included in these figures are $4,007,774 and $3,001,904 respectively which represent the reproduction cost new and the related accumulated depreciation applicable to the tropo-scatter radio system sites at Cartwright and Melville.

3. Depreciation

Commencing July 1, 1966, the provision for depreciation has been accumulated at rates for each class of plant determined by the Company's engineers and approved by the Board of Commissioners of Public Utilities of Newfoundland. Prior to July 1, 1966, depreciation was provided in varying amounts, not exceeding the rate of 3.3% approved by the Board of Commissioners on January 14, 1952, which resulted in an accumulated depreciation deficiency as at June 30, 1966, estimated at $3,390,000.

Effective January 1, 1967 the Company began to amortize the accumulated depreciation deficiency at the rate of $170,000 per annum. This amortization was subsequently cancelled by the Board of Commissioners by its Order No. 6 dated March 27, 1968, ordering the Company to account for the accumulated depreciation deficiency in the following manner:

1) a charge against retained earnings	$ 218,500
2) the elimination of the deferred credits— income tax as at June 30, 1966	1,673,000
3) the setting up of the remaining amount in a special account, which is to be amortized over a period of 20 years commencing on January 1, 1968	1,498,500
	$3,390,000

The depreciation expense for the year ended December 31, 1975 includes $74,925 (1974—$74,925) representing the annual amortization of the amount set up under deferred charges.

4. Unamortized expenses

These expenses represent the cost of station conversions and a physical inventory of the telecommunications property. By Order No. 66 of the Board of Commissioners of Public Utilities of Newfoundland dated October 4, 1966, these expenses are being amortized over periods not exceeding ten years.

5. Capital stock

7.25% cumulative redeemable preferred shares—par value $20 each		
Authorized	250,000 shares	
Outstanding December 31, 1975	232,975 shares	$ 4,659,500
9.75% cumulative redeemable preferred shares—par value $20 each		
Authorized	500,000 shares	
Issued during 1975 for cash	450,000 shares	
Outstanding December 31, 1975	442,915 shares	$ 8,858,300
Ordinary shares—par value $5 each		
Authorized	9,000,000 shares	
Outstanding December 31, 1975	5,082,259 shares	$25,411,295

The 7.25% cumulative redeemable preferred shares may be redeemed by the Company in whole or in part for a redemption price of $21.20 if redeemed on or before September 15, 1978, $21.00 thereafter to September 15, 1981, $20.80 thereafter to September 15, 1984, $20.60 thereafter to September 15, 1987, $20.40 thereafter to September 15, 1990, and $20.20 thereafter.

The 9.75% cumulative redeemable preferred shares were authorized by a special resolution passed by the shareholders of the Company on March 26, 1975, and approved by the Board of Commissioners of Public Utilities of Newfoundland on April 9, 1975.

The 9.75% cumulative redeemable preferred shares shall not be redeemed by the Company prior to May 15, 1980 other than for sinking fund purposes. On and after May 15, 1980 the Company may redeem in whole or in part the preferred shares for a redemption price of $21.40 on or before May 15, 1983, $21.20 if redeemed thereafter and on or before May 15, 1986, $21.00 if redeemed thereafter and on or before May 15, 1989, $20.80 if redeemed thereafter and on or before May 15, 1992, $20.60 if redeemed thereafter and on or before May 15, 1995, $20.40 if redeemed thereafter and on or before May 15, 1998, and $20.20 thereafter.

During the year to December 31, 1975, 6,250 7.25% preferred shares of an aggregate par value of $125,000 and 7,085 9.75% preferred shares of an aggregate par value of $141,700 were purchased for cancellation pursuant to the preferred share purchase fund provisions. As required by the Companies Act (Newfoundland), an equal amount has been transferred from retained earnings to the "capital redemption reserve fund."

6. Retained earnings

As a result of income tax adjustments to the years 1971 to 1974, the balance of retained earnings at December 31, 1974 previously reported as $6,604,349 has been restated to show a retroactive credit of $723,104 representing the cumulative amount by which income taxes as at December 31, 1974 have been decreased. Of the $723,104, $255,643 is applicable to 1974 and has been credited to income for that year. The remaining $467,461 is applicable to periods prior to January 1, 1974 and has been credited to retained earnings previously reported as $5,117, 649.

7. Unsecured Subordinated Notes— due to parent company

Series A Unsecured Subordinated Notes—These unsecured subordinated notes of $9,040,000 (1974—$10,170,000) payable to Bell Canada bear interest at ¼ of 1% above a Canadian chartered bank's prime rate subject to a minimum annual rate of 7% and a maximum annual rate of 9%. These notes mature in equal amounts serially in each of the years ending December 31, 1976 to 1983 inclusive.

Series B Unsecured Subordinated Note—This unsecured subordinated note of $609,941 (1974—$609,941) is to be paid to Bell Canada on December 31, 1983 under the same interest conditions set forth for Subordinated Notes "A".

These notes are redeemable at par without penalty at the option of the Company.

8. Long term debt

First Mortgage Sinking Fund Bonds

Series	Maturity	Issued	Outstanding
5½%	May 15, 1977	$ 1,500,000 (A)	$1,214,000
5½%	June 1, 1978	1,000,000 (A)	840,000
6%	June 1, 1979	1,000,000 (A)	820,000
7%	May 1, 1980	2,000,000 (A)	1,720,000
9¼%	May 15, 1990	7,500,000 (A)	1,357,000
8⅝%	April 15, 1992	7,500,000 (A)	6,900,000
9%	December 1, 1994	15,000,000 (A)	14,400,000
11%	October 1, 1996	17,500,000 (A) (B)	17,500,000
			44,751,000

First Mortgage Bonds

Series	Maturity	Issued	Outstanding
7⅞%	November 1, 1978	500,000	500,000
5½%	June 1, 1988	3,000,000	3,000,000
7%	December 15, 1991	3,000.000	3,000,000
7⅞%	November 1, 1993	2,500,000	2,500,000
			$53,751,000

(A) Each of the eight series of First Mortgage Sinking Fund Bonds has a sinking fund requiring payment by the Company as follows:

(i) Series 5½%, 5½%, 6% and 7%—require payment in each year equal to 1% of the issued aggregate principal amount of each such series.

(ii) Series 9¼%, 8⅝%, 9% and 11%—require payment in each year commencing 1975, 1972, 1974 and 1979 respectively of an amount equal to 2% of the issued aggregate principal amount of each series.

The aggregate amount of payments estimated to be required in each of the next five years to meet maturities and sinking fund obligations of those series of the First Mortgage Bonds of the Company presently outstanding is as follows: $507,400 in 1976, $1,721,700 in 1977, $1,817,700 in 1978, $1,667,700 in 1979 and $2,467,700 in 1980.

(B) The holders of any series 11% Bonds have the right to elect that the Company repay the principal amount of the Bond on October 1, 1979 provided they present the Bonds to the Trustee after October 1, 1978 and prior to April 1, 1979.

9. Notes payable

Demand bank loans (unsecured) outstanding at December 31, 1975, bearing interest at a Canadian chartered bank's prime rate, represent interim financing incurred in the expansion of the Company's operation.

10. Income taxes

In September 1967, the Accounting and Auditing Research Committee of the Canadian Institute of Chartered Accountants recommended the general use of the tax allocation basis of accounting for corporate income taxes instead of the taxes payable basis. The Company agreed with and had been using this generally recommended accounting treatment.

While stating that the general principles of income measurement should apply in the case of regulated industries, the Research Committee recognized that there may be rare cases where the taxes payable basis for regulated industries could be used provided all taxes payable in the future years will be included in the approved rate and will be recoverable from the customer at that time.

In its Order No. 6 dated March 27, 1968, the Board of Commissioners of Public Utilities of Newfoundland did not allow the Company to use the tax allocation basis, and ordered the Company to charge the amount of income tax that would be payable if it claims both the maximum capital cost allowances permitted by the Federal Income Tax Act, and all other items which may be expensed for income tax purposes at a different time from that at which they are expensed for financial statement purposes, except "where the deferment is for a short period." In so ordering, the Board implicitly guarantees that taxes payable in future years will be included in the approved rate and that these taxes will be recoverable from the customer at that time.

On January 29, 1974, the Board of Commissioners approved an exception to its previously stated policy, by permitting the Company to provide, commencing in 1973, as a current operating expense, deferred income taxes on those items, other than capital cost allowances, claimed for tax purposes but not yet charged against income in the financial statements.

In 1975 the Deferred Income Taxes increased by $2,284,388 of which $788,358 was due to re-assessments of income taxes for the years 1971 to 1974 inclusive. These re-assessments resulted from claiming for income tax purposes certain additional expenditures in excess of those included in operating expenses for the respective years.

By continuing to disallow deferred taxes relating to excess capital cost allowances as an operating expense, net income for the year ended December 31, 1975 has been overstated by approximately $1,365,000 (1974—$1,403,000). The cumulative amount to December 31, 1975 by which deferred taxes have been understated and retained earnings overstated is estimated to be approximately $9,400,000 of which $8,350,000 is related to excess capital cost allowance and $1,050,000 is related to other timing differences from January 1, 1968 to December 31, 1972.

Because of the requirement to adhere to the orders of the Board of Commissioners, the financial statements of the Company are not directly comparable with those of other similar companies.

11. Other income

Other income includes interest charged to construction of $623,086 (1974—$525,864) less miscellaneous income charges. The interest charged to construction is also included in the item "Charges to construction not requiring an outlay of funds" in the Statement of Changes in Financial Position.

12. Pensions

The Company has a non-contributory plan which provides for service pensions based on length of service and rates of pay. The last actuarial review of December 31, 1972 indicated that no liability existed in respect of past service pension costs and all vested benefits were fully funded.

13. Remuneration of directors and officers

During the year 1975 the Company was served by 10 directors (1974—11 directors). As such their aggregate remuneration from the Company was $18,450 (1974—$15,900).

The Company had 6 officers during 1975 (1974—5 officers) and their aggregate remuneration as officers was $188,693 (1974—$151,908). Two of the officers served also as directors of the Company, one of whom received no director's fee.

14. Commitments

Material contractual obligations in respect of long term leases on account of real property of the Company amounted to approximately $946,000 at December 31, 1975 (1974—$983, 380). Rentals incurred reflecting real and personal property for the year ended December 31, 1975 amounted to $3,378,700 (1974—$2,520,000), and the estimated amount payable during the five years subsequent to the date of the balance sheet is $13,717,000 (1974—$17,100,000).

15. Anti-inflation legislation

The Company is subject to the Federal Government's anti-inflation legislation, which became effective October 14, 1975.

Although it has not been possible to accumulate the information necessary for the specific calculations required to determine compliance with the legislation, management is of the opinion that the Company has no liabilities with respect to the anti-inflation legislation.

16. Subsequent event

On February 2, 1976 the Company, under a Deed of Trust dated August 1, 1946, issued $10,000,000 in First Mortgage Sinking Fund Bonds bearing an interest rate of 11.5%.

Auditors' Report

The Shareholders,
Newfoundland Telephone Company Limited.

We have examined the balance sheet of Newfoundland Telephone Company Limited as at December 31, 1975 and the statements of income, retained earnings and changes in financial position for the year then ended. Our examination included a general review of the accounting procedures and such tests of accounting records and other supporting evidence as we considered necessary in the circumstances.

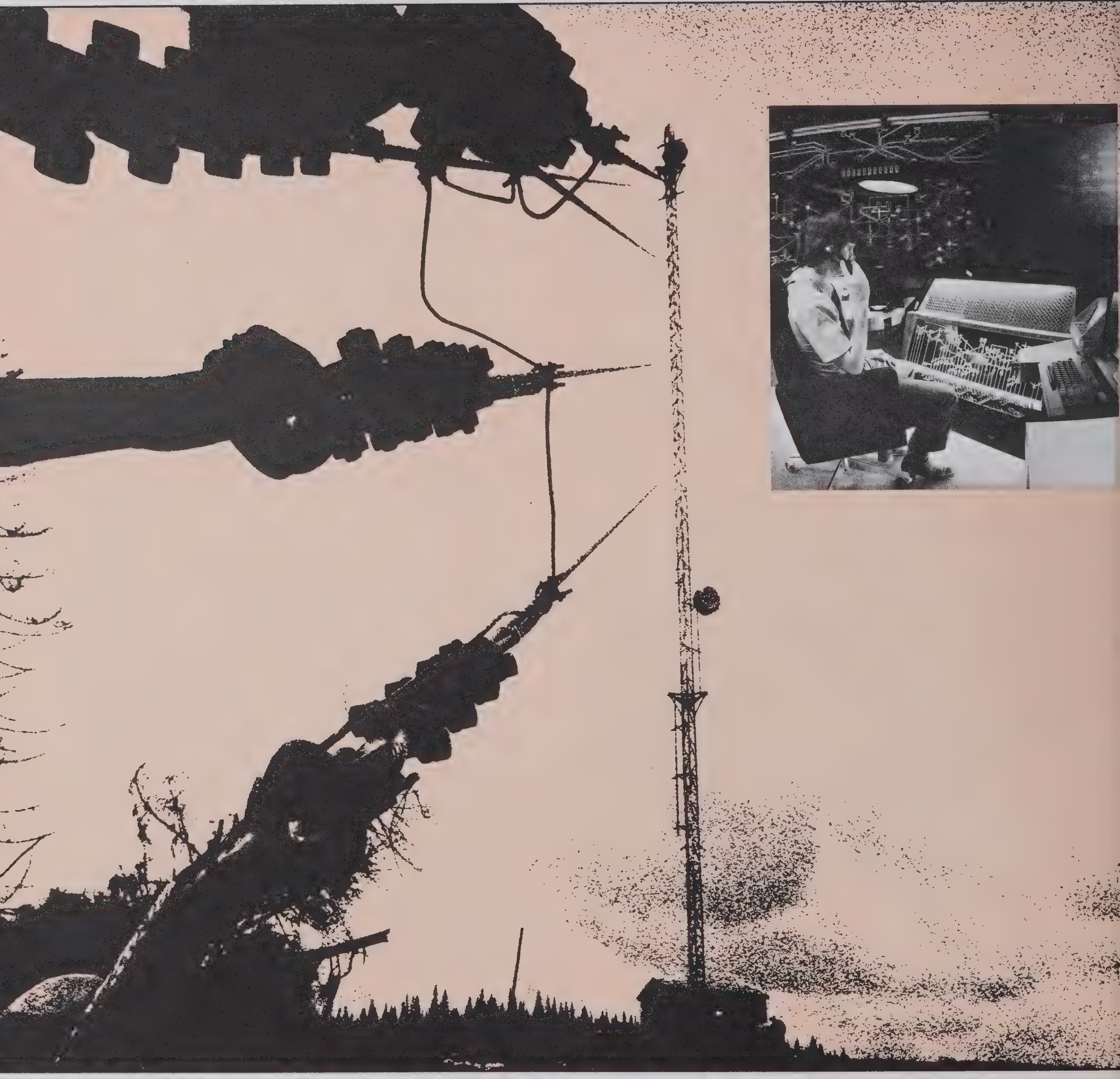
In our opinion these financial statements present fairly the financial position of the company as at December 31, 1975 and the results of its operations and the changes in its financial position for the year then ended, in accordance with generally accepted accounting principles applied on a basis consistent with the restated figures of the preceding year.

Touche Ross & Co.

Chartered Accountants.
Montreal, Quebec.
February 6, 1976.

The Trans-Canada Telephone System microwave spans the country—providing long-distance, broadcasting and data transmission services to every province.

The inset shows the TCTS control center in Ottawa. Staffed by representatives from all TCTS member companies, the center constantly monitors transmission quality and ensures system efficiency.



Trans-Canada Telephone System

The Trans-Canada Telephone System (TCTS) is a consortium of nine major telephone companies, representing every province. The newest TCTS member is Island Telephone of Prince Edward Island, which joined the system in September of 1975.

Together, the TCTS member companies provide a cross-country telecommunications network serving the needs of most Canadians. Besides a high volume of long-distance calling, the network carries radio and television broadcasting, and data in all its forms.

TCTS headquarters are situated in Ottawa. Staffed by personnel from all member companies, the office distributes jointly-earned revenues, and works to establish and uphold technical and operating standards throughout the industry. The system also provides a forum for the companies to exchange information and to consult with one another on many areas of common interest.

The network has continually expanded since its formation in 1931. In 1975, TCTS constructed the world's longest stereo network, stretching from St. John's to Vancouver. This project made TCTS the prime carrier of TV, AM and FM broadcasting for the CBC, which is providing the stereo programs to major cities across Canada.

The foundation of the System's business is shared long-distance revenues from calls which use the facilities of three or more member companies. This traffic totalled close to 134,474,000 messages for the year showing an increase of about 25% in gross revenue for 1975. Part of the increase in revenue was the result of a new rate schedule implemented in August. Continued growth in both local and long-distance calling was reflected by the construction budgets of member companies, which exceeded $1.5 billion in 1975, and is expected to pass the $2 billion mark by 1977.

All member companies sought increases in rates during 1975. Since the soaring costs of energy and transportation have boosted use of telecommunications, there is a pressing need for the industry to continue a high level of construction—and a corresponding need for increased revenues to meet spiralling construction costs.

The Computer Communications Group of TCTS continued to expand its Dataroute transmission service during the year. Launched in 1973, The Dataroute was the first nationwide digital data system in commercial operation. By November of 1975, there were 29 cities across Canada served by the system.

A major effort in telecommunications continues to be the universal common carrier network for computer communications, as opposed to the discrete network set up for a single customer. The same logic that led to a universal telephone network accessible to any caller, will lead to the establishment of a universal network for computer communications. In consultation with other worldwide carriers, and with the CCITT (Consultative Committee on International Telegraphy & Telephony), TCTS has developed a Standard Network Access Protocol which is the first step toward such a universal system.

Ten Year Statistical Record

	1975	1974	1973	1972
Telephone Service Facts				
Number of telephones	150,369	142,058	123,157	109,829
Per cent dial	100	99	99	97
Local calls—daily average	2,146,158	1,949,919	1,690,456	1,516,542
Long distance calls—daily average	30,396	26,052	20,594	17,534
Income				
Total operating revenues	$ 43,092,044	35,507,716	26,177,774	22,207,582
Total operating expenses and taxes*	$ 31,398,579	25,764,793	19,606,794	16,020,843
Interest charges	$ 7,106,774	5,599,005	2,845,919	2,399,889
Net income before extraordinary item*	$ 5,218,302	4,760,876	3,892,860	3,839,711
Extraordinary item	$ —	—	—	—
Net income*	$ 5,218,302	4,760,876	3,892,860	3,839,711
Selected Balance Sheet Items				
Investment in plant and equipment	$169,422,806	146,343,959	94,182,627	79,419,848
Total long term debt	$ 81,800,941	75,244,941	43,804,000	30,802,000
Shareholders' equity*	$ 48,770,279	38,514,735	36,772,392	35,870,912
Financial Ratios				
Earnings per average ordinary share*	$ 0.85	0.87	0.70	0.74
Dividends per ordinary share	$ 0.50	0.50	0.50	0.50
Equity per ordinary share*	$ 6.84	6.64	6.27	6.07
Per cent long term debt to total capitalization	62.6%	66.1%	54.4%	46.2%
Rate of return on average total capital*	10.10%	10.10%	9.15%	9.81%
Interest in per cent of average debt	9.06%	9.41%	7.63%	7.81%
Times interest earned before taxes*	2.41	2.56	3.81	3.54
Other Statistics				
Construction expenditures	$ 27,323,473	28,614,346	16,243,036	10,610,682
Plant investment per telephone	$ 1,127	1,030	765	723
Number of employees	1,278	1,324	1,124	953
Salaries and wages paid	$ 13,583,388	10,763,803	7,787,214	6,216,497

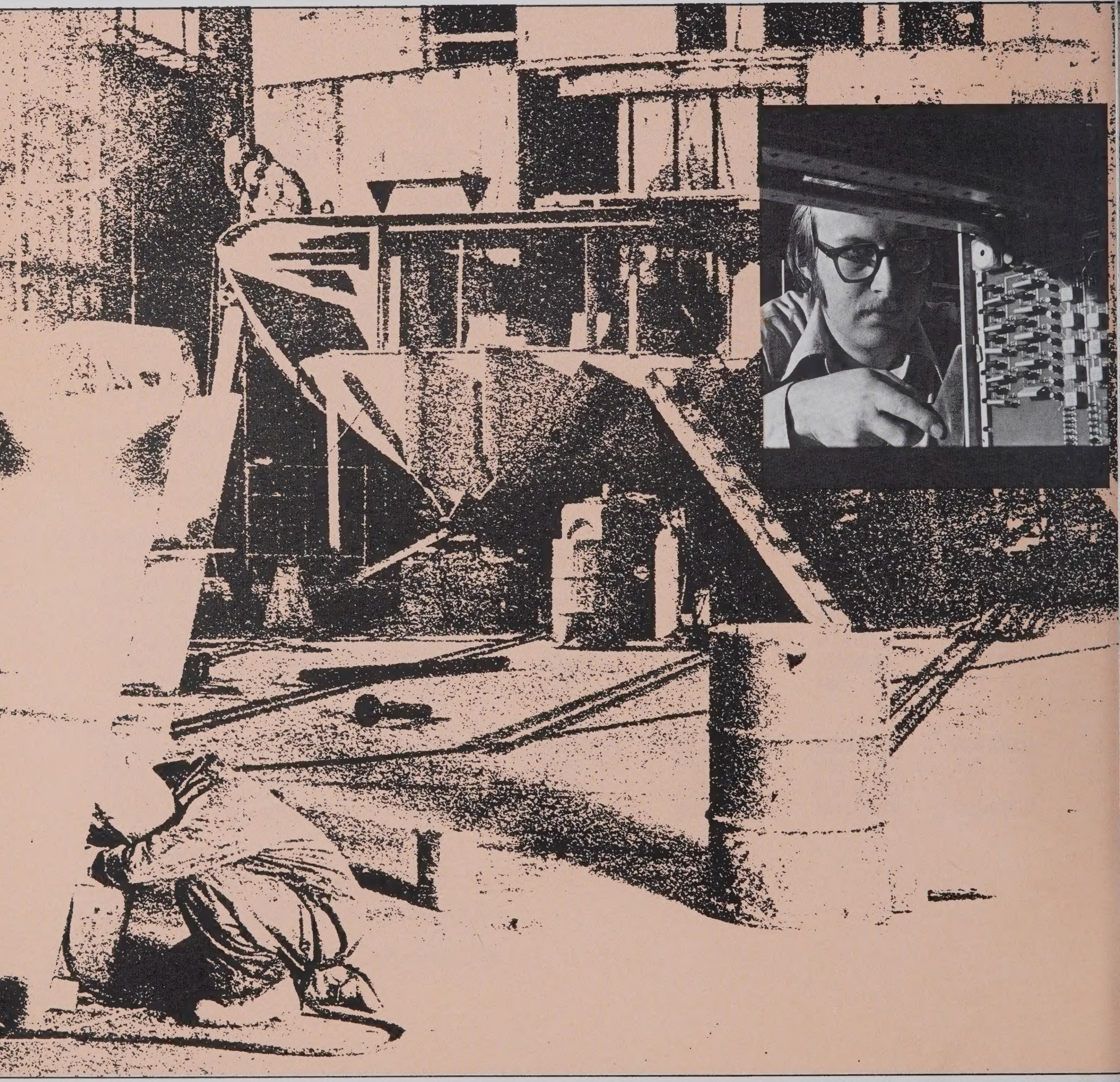
***Results Reflect**
(1) Tax allocation basis for 1966 and 1967
(2) Tax payable basis for 1968 to 1972
(3) Partial tax allocation basis for 1973 to 1975

1971 to 1974 have been restated where applicable.

1971	1970	1969	1968	1967	1966
100,664	92,991	88,247	82,645	76,218	69,285
97	96	95	94	92	92
1,290,705	1,108,248	979,179	849,092	732,945	615,023
15,068	14,384	13,562	12,619	11,137	9,976
19,174,109	17,450,266	13,261,627	11,675,793	10,303,609	7,504,656
13,779,261	13,038,440	10,271,669	8,661,571	7,480,518	6,094,823
2,209,441	2,035,149	1,876,109	1,719,395	1,460,311	1,375,248
3,243,786	2,590,230	1,145,504	1,365,683	1,416,032	96,865
—	1,113,850	355,181	471,538	14,068	—
3,243,786	3,704,080	1,500,685	1,837,221	1,430,100	96,865
70,020,022	62,475,742	55,379,535	50,393,805	45,931,159	39,013,617
30,659,000	25,841,000	24,526,500	24,357,000	24,187,000	23,223,089
29,885,785	28,954,427	23,733,468	20,549,286	17,272,722	13,255,621
0.64	0.80	0.37	0.52	0.46	0.04
0.45	0.41	0.40	0.40	0.20	—
5.88	5.70	5.34	5.39	5.44	5.21
50.6%	47.2%	50.8%	54.2%	58.3%	63.7%
9.46%	11.14%	7.25%	8.24%	7.38%	4.35%
7.82%	8.08%	7.68%	7.08%	6.16%	6.66%
3.23	4.84	3.03	3.90	3.21	1.25
8,642,025	8,044,828	6,514,027	6,708,206	8,192,854	4,525,251
696	672	628	610	603	563
877	824	849	835	867	819
5,284,000	4,632,144	4,073,949	3,385,373	3,405,006	2,810,461

Newfoundland's tomorrow has started today. A recent government study of the economic outlook for the province has concluded that "most sectors should experience real growth in 1976".

An effective telecommunications system is an important pre-requisite of economic growth. Your company has anticipated and prepared for the demands of today ... and tomorrow.



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St. John's, Nfld.

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President & Managing Director
Newfoundland Telephone Company Limited
St. John's, Nfld.

H. Collingwood
Chairman & President, Baine Johnston & Co. Ltd.
St. John's, Nfld.

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Vice-President & Comptroller, Bell Canada
Montreal, Quebec

H.L. Lake
Executive Vice-President, The Lake Group Ltd.
St. John's, Nfld.

A.R. Lundrigan
President, Lundrigans Ltd.
Corner Brook, Nfld.

The Hon. F.A. O'Dea, Q. C.
Legal Counsel
St. John's, Nfld.

F.J. O'Leary
Chairman, The St. John's Housing Corporation
St. John's, Nfld.

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Ottawa, Ontario

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Vice-President—Operations

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Secretary

D. Adey
Treasurer & Assistant Secretary

D.G. Wright
Comptroller